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BEFORE THE ARIZONA CORPORATION COMMISSION

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KRISTIN K. MAYES, Chairman
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AZ CORP COMMISSION
DOCKET CONTROL

IN THE MATTER OF THE REVIEW AND
POSSIBLE REVISION OF ARIZONA
UNIVERSAL SERVICE FUND RULES,
ARTICLE 12 OF THE ARIZONA
ADMINISTRATIVE CODE.

DOCKET NO. RT-00000H-97-0137

IN THE MATTER OF THE INVESTIGATION OF
THE COST OF TELECOMMUNICATIONS
ACCESS.

DOCKET NO. T-00000D-00-0672

NOTICE OF FILING

REPLY BRIEF OF THE ARIZONA LOCAL EXCHANGE CARRIERS ASSOCIATION

The Arizona Local Exchange Carriers Association ("ALECA") hereby files its Reply
Brief in the above-captioned dockets.

RESPECTFULLY SUBMITTED on September 14, 2010.

Arizona Corporation Commission

DOCKETED

SEP 14 2010

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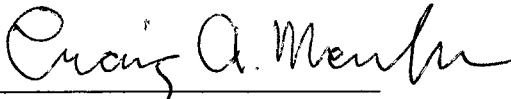
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**REPLY BRIEF
OF THE
ARIZONA LOCAL EXCHANGE CARRIERS ASSOCIATION**

I. INTRODUCTION

1. Access-Charge Reform

The AUSF-reform docket has been pending for more than 13 years. The Access-charge reform docket has been pending for ten years. ALECA has been diligently pushing for reform in both dockets.

Although ALECA can largely be credited with encouraging this case to conclusion, many of the parties seem to be doing their best to support the old adage; "No good deed goes unpunished."

Sprint would immediately reduce the ILEC's intrastate access rates to the interstate access rates. This would immediately reduce the ILEC's revenues by millions of dollars, but Sprint would not provide any relief other than a vague opportunity to make up the revenues

1 through non-jurisdictional services. Sprint's self interest is obvious, as is its disregard for the
2 financial future of Arizona's rural ILECs and the customers they serve.

3 Cox and the Joint CLECs first argue that the Commission should wait for the FCC to act,
4 but if the Commission is determined to act, it should first deal with the rural ILECs. They
5 provide only vague lip service to making the rural ILECs whole in that event.

6 Qwest would do nothing to further reduce its own rates. However, it asks the
7 Commission to immediately reduce intrastate access rates for rural ILECs. To its credit, it does
8 propose a method to allow the rural ILECs to offset the lost revenues, but, as discussed below, it
9 would fall far short of providing complete relief.

10 Staff appears to support rate relief for rural ILECs as part of access-charge reform, but
11 the process would be extremely time consuming and would require each rural ILEC to prepare,
12 file, and prosecute a rate case, imposing considerable burden on staff and others' resources.

13 RUCO opposes any kind of revenue-neutral rate relief if the Commission decides to
14 reform rural ILECs' intrastate access rates.

15 Only Verizon and AT&T seem genuinely interested in promoting access-charge reform,
16 while doing no harm to the rural ILECs.

17 **2. AUSF Reform**

18 Although AUSF Reform has been part of this case for over 13 years, Staff inexplicably
19 states that considering it would unduly broaden the scope of issues in this case.

20 It is very difficult to understand the aversion that the parties in this case have to
21 increasing the AUSF. In contrast to other states, Arizona's AUSF program can only be
22 considered a failure. Only one company receives AUSF support, and the total statewide budget
23 is just \$769,720.¹

24 ALECA proposes to expand the AUSF to supplement the Federal high-cost loop support.
25 ALECA's members do not have a large enough customer base to recover a sufficient amount of

¹ Tr. at 684:19 – 685:7.

1 revenue to cover the cost of providing local service. Local service revenues and access revenues,
2 which have been designed to keep local service rates affordable, are used to recover loop costs
3 that do not exceed the 115 percent NACPL threshold. Under ALECA's high-cost loop proposal,
4 all loop costs above this threshold would be recovered through either the existing federal HCL
5 mechanism or through the new State high-cost loop mechanism.

6 No party has offered any cogent reason why the AUSF should not be modestly expanded
7 to support rural ILEC's costs to provide service. No party has suggested that this is not a proper
8 purpose for the AUSF. The Commission should approve ALECA's modest proposal.

9 ALECA also recommends that the Commission adopt the proposals contained in the
10 Report and Recommendations of the Eligible Telecommunications Carriers ("ETC"s) on Lifeline
11 and Link-Up Issues, docketed December 21, 2005. The modest cost of central administration
12 would be just over \$325,000 per year, which would go directly to DES, and could generate as
13 much as \$38 million in additional customer support.² This is a return of \$114 for every dollar of
14 AUSF support.

15 **II. ACCESS REFORM**

16 **1. Qwest Proposal**

17 ALECA still believes that its access-reform proposal strikes the best balance between the
18 interests of their customers and other parties in the case. However, with modifications, ALECA
19 could support Qwest's access-reform proposal.

20 As ALECA understands it, Qwest's access-reform proposal for rural ILECs is as
21 follows:⁴

- 22 1. All rural ILECs and CLECs should reduce their intrastate access to Qwest's intrastate
23 access rate.
- 24 2. Carriers should be permitted to increase end user rates to a statewide benchmark as a
25 first step to off-setting the reduction in intrastate access revenues.

² Tr. at 688:20 – 689:1.

⁴ Qwest Brief at 10:1-7.

1 3. To the extent that increasing local rates is insufficient for revenue neutrality, the
2 AUSF may be utilized if the carrier undergoes a simplified earnings review.

3 “Qwest recommends that that the residential benchmark rates be set at 125 percent of the
4 weighted average Arizona residence rate and the business benchmark be set at 125 percent of the
5 weighted average Arizona business basic exchange rates.”⁵ For residential customers, the Qwest
6 benchmark would be \$16.45/month.⁶

7 Qwest’s proposal has merit, but would require modifications to be acceptable to ALECA.
8 First, rural ILECs would immediately reduce intrastate access rates to Qwest’s intrastate access
9 rate while simultaneously increasing end-user rates to the state-wide benchmark. This would
10 only work if the rate increase to the benchmark would offset the revenues lost by the access-
11 charge reduction. Otherwise, the ILEC would have to endure months of revenue reductions with
12 no offsetting revenue make-up.⁷

13 The second issue with Qwest’s proposal is that many of ALECA’s members would be
14 unable to recover lost access-charge revenues by increasing local rates to Qwest’s \$16.45/month
15 benchmark. The current weighted residential local rate for ALECA members is \$12.91/month.⁸
16 Mr. Shand testified that “the residential local exchange service rates for the rural incumbent
17 LECs range from \$9.25 to \$24.46 per month.”⁹ However, to reduce access-charge rates to
18 Qwest’s level would require the average rural ILEC to increase local rates by \$10.74/month.
19 There is just not enough head-room between existing residential rates and Qwest’s \$16.45/month
20 benchmark to make ALECA members whole. And ALECA members with rates above the
21 Qwest \$16.45/month benchmark would be unable to recover any of their foregone revenues.

22 ALECA could accept a modified Qwest proposal, as follows:

⁵ Direct Testimony of Peter B. Copeland at 4:13-16.

⁶ AT&T Brief at 39:3-4.

⁷ Although it is not clear if this is Qwest’s final proposal, Mr. Copeland does describe a revenue-neutral phase down in his direct testimony. Direct Testimony of Peter B. Copeland at 7:10-13.

⁸ Reply Testimony of Douglas Duncan Meredith at 6:22 – 7:1.

⁹ Direct Testimony of Wilfred Shand at 18:12-14; WS-2.

- 1 1. **Higher Benchmark Rate.** The first remedy for Qwest's proposal would be to use a
2 higher residential benchmark rate. AT&T proposes using a benchmark set at
3 \$18.00/month (still less than \$19.53, which is 125% of the national retail average of
4 \$15.62).¹⁰
- 5 2. **Capped Access Charge Reductions.** The second remedy would be to cap initial
6 access charge reductions at the level that could be offset by increasing residential
7 rates up to the \$18.00/month benchmark rate, or by 35%, whichever is less. This
8 would allow the access-charge reductions to be revenue neutral and would allow even
9 the rural ILECs with higher-than-average local rates some ability to reduce access
10 charges without huge rate increases.
- 11 3. **Rate Flexibility.** As just discussed, access charges for each rural ILEC would be
12 reduced by an amount equal to the lesser of (1) the revenue difference between
13 existing residential rates and the \$18/month benchmark, and (2) the amount generated
14 by a 35% residential rate increase. Some companies may not want to fully offset this
15 decrease through rate increases, so ALECA asks that companies not be required to
16 increase rates to the maximum extent allowed. In other words, rural ILECs would be
17 required to reduce access rates by the full amount calculated by the above
18 methodology, but would not be required to increase residential rates by the full
19 allowable amount.
- 20 4. **Centralized Administration of Lifeline and Linkup.** To minimize the impact on
21 low-income customers of residential rate increases allowed to offset access charge
22 reductions, the Commission should support ALECA's proposal to centralize
23 administration of Lifeline and Linkup. As discussed below, centralized enrollment is
24 an extremely effective method of increasing the availability of these benefits to
25 eligible customers.

¹⁰ AT&T Brief at 37:11-13:5-9.

1 5. **Pass-Through of Access-Charge Reductions.** To ensure that rural customers get
2 the full benefit of access-charge reductions, intrastate carriers should be required to
3 pass through on their bills the full amount of access-charge reductions, and
4 demonstrate to the Commission the rate reductions that correspond to access charge
5 reductions.

6 ALECA understands that the modified Qwest proposal would not provide full access-
7 charge reductions for all rural ILECs. However, it would be a strong first step and would not
8 unduly burden retail customers.

9 For a second step, a rural ILEC would be allowed to apply for AUSF support to offset
10 further access-charge reductions. The company would file sufficient information to allow the
11 Commission, after a streamlined proceeding, to determine fair value and quantify the necessary
12 AUSF support.

13 **2. Staff's Access-Charge Proposal is Unworkable**

14 Staff recommends that the Commission order rural ILECs to reduce their intrastate
15 access-charges to the greater of Qwest's intrastate access-charge rate or the ILEC's interstate
16 rate.¹¹ However, Staff acknowledges that access-charge rate reductions cannot be made without
17 first completing a rate case for the subject company.¹² To process all these cases, Mr. Shand
18 agrees, "would take some time."¹³

19 Realistically, processing rate cases for all the rural ILECs would take at least two years.¹⁴
20 Given that a final order in this case is unlikely before the first quarter of 2011, access-reform
21 would be delayed until 2013, or even later. If a rulemaking is first needed, then access-charge
22 reform might not be effective until 2015. Thus, there is ample reason to believe the FCC's

¹¹ Staff Brief at 7-9.

¹² Tr. at 664:12 – 665:4; 691:8 – 692:4.

¹³ Tr. at 665:9.

¹⁴ Staff's alternative proposal contemplates that the last rate case would not even be filed until 42 months after a decision in this docket. Shand Direct at 27-28.

1 actions in regard to intercarrier compensation may be completed before or only shortly after the
2 ACC could complete a rulemaking and multiple ALECA rate cases.

3 ALECA's proposal would allow access-charge reform immediately after a rulemaking is
4 completed. Qwest's proposal, if modified as suggested by ALECA, could allow access reform
5 even sooner.

6 **3. Reply to Other Parties**

7 **A. Revenue-Neutral Access Charge Modifications are Constitutional**

8 RUCO argues that it would be unconstitutional to make up access charge reductions by
9 increasing rates, unless the Commission made a new fair-value finding.¹⁵ This is incorrect. Staff
10 cites *Scates v. Arizona Corporation Commission*, 118 Ariz. 531, 578 P.2d 612 (App. 1978), to
11 support its position that "a change to other rates of the company could be made to offset the
12 switched access charge reduction as long as the change in rates was overall revenue neutral
13 outside of a rate case." ALECA agrees with Staff's analysis.

14 **B. Rural ILECs Cannot Make Up Access Charge Reductions Through**
15 **Non-Jurisdictional Revenues**

16 Sprint claims that rural ILECs could make up revenue lost through access charge
17 reductions with revenue from non-jurisdictional sources such as long distance, broadband, and
18 video services.¹⁶ The Commission should ignore this claim for three reasons.

19 First, the Commission sets local rates based on jurisdictional cost of service and
20 revenues. It cannot consider revenue from services provided at rates set not established by the
21 Commission.

22 Second, Sprint has provided no meaningful evidence that rural ILECS have any ability
23 whatsoever to offset access charge reductions from non-jurisdictional sources. To do this would
24 require the Commission to determine, on a company-specific basis, all revenues received from

¹⁵ RUCO Brief at 8:1-18.

¹⁶ Sprint Brief at 27:20 – 30:1.

1 these sources, and, all costs required to provide these services, something which, by virtue of the
2 services being NON-jurisdictional, it could not do.

3 Third, Sprint ignores the competitive market realities of providing long distance,
4 broadband, and video services. In today's competitive communications market, it is naïve to
5 suggest that increasing rates on these services is a reasonable way to recover mandatory rate
6 reductions on regulated services.

7 **III. AUSF REVISIONS**

8 **1. AUSF Rule Revisions Are Clearly Within the Scope of this Case**

9 Before discussing ALECA's AUSF proposals, Staff incredibly argues that the scope of
10 this case should not be broadened beyond access-charge reform.¹⁷ The scope of this case does
11 not need to be broadened to discuss ALECA's AUSF proposals.

12 This case began more than 13 years ago in Docket No. RT-00000H-97-0137. The case
13 caption is: "In the Matter of the Review and Possible Revision of Arizona Universal Service
14 Fund Rules, Article 12 of the Arizona Administrative Code." Possible AUSF rule revisions have
15 always been part of this case.

16 Staff should be well aware that there are two dockets worth of issues to be considered.
17 On July 10, 2007, Staff moved to consolidate the AUSF-review and access-charge dockets: (RT-
18 00000H-97-0137 and T-00000D-00-0672).¹⁸ Staff's Motion was granted by Procedural Order
19 Dated September 19, 2007.

20 On September 4, 2007, Staff filed a revised list of AUSF issues it thought should be
21 considered in the consolidated dockets, including

- 22 6. What revisions to the existing AUSF rules should be made?
- 23 11. Should companies be required to file a rate case to obtain AUSF revenues?
- 24 12. If a rate case is not required, what method should be used to determine whether a
- 25 company should receive AUSF payments?

¹⁷ Staff Brief at 6:14.

¹⁸ Staff's July 10, 2007, Motion to Consolidate Dockets and Request for Procedural Conference.

- 1 13. Should the AUSF rules be amended to allow for the provision of telephone
- 2 service in unserved or underserved areas?
- 3 14. Should the AUSF rules be amended to allow for incentives to companies to the
- 4 provide telephone service in unserved or underserved areas?
- 5 15. Should the AUSF rules as proposed by ALECA be adopted?

6 On November 19, 2007, Staff filed a Notice of Filing, including an additional list of
7 issued relating to the possible revisions to the AUSF, stating that it had prepared additional
8 AUSF questions relating to Lifeline and Linkup. The filing referenced "the Report and
9 Recommendations of the Arizona Eligible Telecommunications Carriers ("ETCs") on Lifeline
10 and Link-Up Issues ("ETC's Report") which was filed on December 21, 2005 in Docket No. T-
11 00000A-05-03802," and included the following additional issues that should be addressed in
12 these dockets:

- 13 21. Should a program to improve participation in Lifeline and Link-Up be supported
- 14 by AUSF?
- 15 22. Should the enrollment program recommended by the ETCs be implemented or is
- 16 there another more cost effective method for increasing Lifeline and LinkUp
- 17 participation?
- 18 23. Is the funding mechanism for the enrollment program recommended by the ETCs
- 19 appropriate, should the cost be borne by the ETCs as a cost of doing business and
- 20 being an ETC or is the some other method of funding that would be better?
- 21 24. Are the projections for potential Lifeline and Link-Up customers reasonable or is
- 22 there other data that would increase or decrease the cost/benefit estimates
- 23 contained in the ETC's Report? Please provide such data.
- 24 25. Should the recommendations in the ETC's Report be implemented, how should
- 25 the AUSF rules be modified to address the enrollment program and the payments
- 26 that would be made to the Department of Economic Security ("DES") for its
- 27 participation?

28 Finally, ALECA's two AUSF proposals are well within the scope of the procedural
29 orders in these dockets. The November 30, 2007, Procedural Order directed "that interested
30 entities shall file any Initial Comments concerning possible revisions to the AUSF Rules ... no
31 later than January 7, 2008. On that date, ALECA filed its Initial Responses to Staff's Lists of
32 Issues. ALECA's Initial Responses thoroughly discussed its two AUSF proposals, which were
33 not materially different from those proposed in Mr. Meredith's direct testimony on ALECA's

1 behalf.¹⁹ Then, on February 4, 2008, ALECA filed its "Reply Comments to Staff's List of
2 Issues."

3 The Commission's February 14, 2008, Procedural Order then set-forth a process to
4 possibly reach consensus on Staff's issue list, noting: "The parties have expended significant
5 effort in filing their comments with the Commission and it is important that the Commission
6 continue to move forward with its investigation of potential reform of universal service funding
7 and access charges."²⁰

8 The Commission's February 3, 2009, Procedural Order then ordered that Staff hold a
9 series of workshops concerning the various issues raised by the parties. ALECA dutifully
10 participated in the workshops and again set forth its two AUSF proposals concerning State high-
11 cost loop support, and centralized administration of Life Line/Link-Up.

12 The Commission's September 30, 2009, Procedural Order summarized the process over
13 the previous two years:

14 In the two years since the consolidated dockets were re-activated, the Commission
15 has grappled with how best to proceed with its investigation into access charges
16 and AUSF. There does not appear to be a dispute that access charges and AUSF
17 should be reviewed to reflect the current realities in the communications industry,
18 but after years of discussions among the parties, discovery and workshops, no
19 consensus has emerged about how to proceed, much less on the substantive or
20 policy questions.²¹

21 The Procedural Order clearly notified all the parties, including Staff, that ALECA's two
22 AUSF proposals were still at issue. Issue 10 to be addressed at hearing was:

23 What should be supported by AUSF? Access replacement only? High cost
24 loops? Line extensions? Centralized administration and automatic enrollment for
25 Lifeline and Link-up?²²

26 Finally, Staff was provided every opportunity to ask ALECA's witness any questions it
27 had concerning ALECA's two AUSF proposals.

¹⁹ Exhibit ALECA-1, Direct Testimony of Douglas Duncan Meredith.

²⁰ Procedural Order dated February 14, 2008, at 2:7-9.

²¹ Procedural Order dated September 30, 2009, at 3:22-27.

²² *Id.* at 5:15-17.

1 ALJ RODDA: And I will just ask generically, I won't go one by one, but
2 to see that you have all had an opportunity to ask all the witnesses whatever
3 questions you wanted to ask and thought you had a fair process in this proceeding.

4 (No oral response.)

5 ALJ RODDA: And I will just note for the record that parties are shaking
6 their heads yes, and I would expect if anyone thought otherwise they would let me
7 know if they need additional process.²³

8
9 MR. GRANT: No.

10
11 ALJ RODDA: I am not hearing any. So thank you all. I look forward to your
12 briefs. And that is it. Thanks.

13 There can be no doubt that ALECA's two AUSF proposals (State high-cost loop support;
14 and centralized administration of Life Line/Link-Up) are well within the scope of Staff's issues
15 lists and subsequent procedural orders. There can also be no doubt that Staff and every other
16 party has had ample time and opportunities to evaluate the two AUSF proposals and to take
17 positions concerning them. Staff cannot fairly state that the scope of this case does not include
18 ALECA's two AUSF proposals or suggest that they are not ripe for Commission consideration.

19 **A. State High-Cost Loop Support**

20 With the exception of Qwest, there was nothing in any party's brief concerning AUSF
21 High-Cost Loop Support that has not already been covered in ALECA's initial brief. Qwest
22 maintains that it would be improper to use the federal benchmark of 115% of national average
23 loop costs.²⁴

24 There is nothing improper with using the federal benchmark. It simply determines
25 whether rural ILECS are eligible for federal support, which funds only a portion of the amount
26 exceeding 115%.²⁵ ALECA's proposal would merely use the AUSF to fund the amount not
27 funded by the federal program.

²³ Tr. at 730:9-22.

²⁴ Qwest brief at 33:14 – 34:6.

²⁵ Direct Testimony of Douglas Duncan Meredith at 9-10.

1 Because more of the incremental cost to serve these expensive customers would be
2 provided by the AUSF, there would be less pressure on local rates. Otherwise, local rates would
3 have to increase for all customers to recover the costs to serve these high-cost rural customers.

4 If local rates cannot be increased and more AUSF support cannot be provided, the ability
5 of the ALECA companies to provide advanced services to high-cost customers may be
6 impacted.

7 **B. Centralized Administration of Life Line/Link-Up**

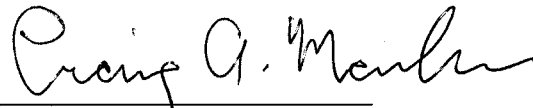
8 ALECA recommends that the Commission adopt the proposals contained in the Report
9 and Recommendations of the Eligible Telecommunications Carriers (“ETC”s) on Lifeline and
10 Link-Up Issues, docketed December 21, 2005. In this report, the ETCs recommended that the
11 Department of Economic Security (“DES”) centrally administer the Lifeline and Link-Up
12 programs of all of Arizona’s ETCs and that the DES be reimbursed for the administrative costs
13 incurred from the AUSF. Centralized administration enables automatic enrollment, and as the
14 ETCs recognized, automatic enrollment is a very effective, if not the most effective, form of
15 outreach.²⁶

16 The modest cost of central administration would be just over \$325,000 per year, which
17 would go directly to DES.²⁷ Staff does not dispute that this modest investment could bring in
18 \$38,000,000 in annual Lifeline and Linkup support. This is a return of \$114 for every dollar of
19 AUSF support. Yet Staff inexplicably still does not support a tiny increase in the AUSF, even
20 for such a worthwhile purpose.
21

²⁶ *Id.*, pp. 11-12.

²⁷ Tr. at 688:20 – 689:1.

1 RESPECTFULLY SUBMITTED on September 14, 2010.
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